

Capstone Comments

A forum for communicating information about the management of assets

Q:
A:

Are bonds still an appropriate investment?

The last twelve months have generated an increased number of financial articles proclaiming the “Death of Bonds”. Prognosticating pundits defend their forecast that bond holders will experience a decrease in the value of their bonds as historically low interest rates begin to rise. The relationship to rising interest rates and decreasing bond values is a financial principal. However, the speculative forecast of the financial “experts” requires their conclusion to be correct twice. First, the “experts” must be right on guessing the event that will influence bond prices and interest rate changes. Second, they must guess correctly how investors will respond to the event.

Last year Bill Gross, Managing Director and Co-Chief Investment Manager of PIMCO, LLC guessed correctly that US Treasuries would be downgraded by the rating agencies. Their second conclusion was wrong. World investor flight to quality of US Treasuries drove the value of Treasuries up. Mr. Gross publicly apologized last October for missing out on last summer’s Treasury rally.

For many investors, bonds remain an important component of a well-diversified portfolio. Bonds and bond funds serve as a shock absorber for the desired higher risk that comes with the return of owning quality American and international companies.

On August 13, 1979, the cover of Business Week infamously proclaimed “The Death of Equities”. That day the Dow Jones Industrial Average stood at 875. Twenty years later the index was 10,973. Fortunately to have a successful long term investment experience, one starts with an investment plan: an appropriate balance of bonds and equities. The plan is monitored, measured and periodically modified through the discipline of rebalancing the portfolio.

Next month, we will explain the relationship between bond prices and interest rates. In the meantime, please feel free to contact us with any questions regarding bonds and their behavior in this environment.

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If you have questions that you think would be interesting for our readers, please call Kerrie at 406-325-1500 or email your questions to kkern@capstoneretire.com.